# Event summary of Session 1

## Introduction of forensic accounting

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## A. Introduction of forensic Accounting

### What does Forensic mean?

- Forensic science is the application of science to criminal and civil laws, as governed by the legal standards of admissible evidence and criminal or civil procedure.

- Forensic scientists collect, preserve, and analyse scientific evidence during the course of an investigation.

- Forensic scientists testify as expert witnesses in both criminal and civil proceedings, or even in the context of alternate dispute resolution mechanisms; ensuring that the relevant evidence is preserved is also one of the duties of forensic scientists.

### What are forensic accountants?

- They are financial professionals who seek to establish the facts of a case, normally to confirm or refute allegations of wrongdoing.

- They work closely with lawyers on the cases on complex accounting issues or financial implications, with the main roles to

  - ✓ analyse, interpret and summarise accounting / financial data but also all relevant surrounding data;

  - ✓ explain complex financial issues in a clear and concise way. Somehow these issues may not be so obvious and understandable to other industry practitioners though they are highly educated.

  - ✓ deal in fact rather than opinion. Forensic practitioners draw conclusions based on the identified facts.

- They may work in

  - ✓ professional accounting practices

  - ✓ private industry and entities, such as compliance departments or banks or internal investigation roles

  - ✓ government and public sector bodies, such as the SFC, ICAC and the police.

### Characteristics and skills of a forensic accountant

While it is not necessary to have all of the following characteristics and skills in order to become a forensic accountant, some common qualities of a good forensic practitioner include:

- analytical

- inquisitive, as the relevant parties may try to hide some facts from you, impacting your investigation process
- detail-oriented; a trivial item may have affected your final investigation result significantly
- able to think out of the box
- persistent; a forensic accountant may not obtain the required information from the relevant parties, and may need to demonstrate persistence in following up
- ethical
- having good communication skills
- confident, to act based on your practical training
- insightful
- responsive
- sceptical; a forensic accountant cannot simply believe the version of "facts" as presented
- creative, and able to find new ways of doing things in view of the ever-changing business environment
- organised and able to manage a complex case or project
- having sound professional judgement, to be able decide, for example, whether or not a piece of information is relevant and significant

**Common career paths for forensic accountants**

- Accounting firms
- Law enforcement, e.g. the Police Force
- Regulatory bodies, e.g. ICAC, SFC and the Insurance Authority
- Banks and financial institutions that have dedicated investigation teams
- Major corporations, e.g. airlines and pharmaceutical companies
- Law firms; there may more forensic practitioners housed within lawfirms in Hong Kong in due course, which is a trend in the U.K.

**A wide range of forensic services**

- Investigations of, for example, fraud, non-compliance, employee misconduct
- Dispute resolution and litigation support, e.g. expert witness work from the financial perspective
- Anti-bribery and corruption expertise, for example, investigating whether there are any issues under the U.S. Foreign Corrupt Practices Act, which prohibits U.S. citizens and entities from bribing foreign government officials to benefit their business interests, or issues under the U.K. equivalent, the Bribery Act.
- Compliance advisory
- Fraud risk assessment and management, e.g. advising on fraud prevention measures
- Business intelligence and asset tracing, such as tracing stolen or concealed assets Computer forensic services to deal with online scams, not necessarily performed by the forensic accountants but who may work with technological experts to get hold of the relevant evidence.
- Data analytics, e.g. identifying and analysing underlying patterns of relevant activities
- Conducting enquiries and cyber Rrisk assessments, particularly in the aftermath of COVID-19

## B. Forensic Framework

**What are the main problems addressed?**

- Fraud
- Financial Crime
- Competition and anti-trust practices
- Contract compliance
- Litigation/ dispute support

**Overall framework for forensic work**

The framework basically includes three aspectsd, namely prevention (e.g. minimising the risk of fraud occurring), detection (e.g. identifying where acts of fraud have happened) and the response (e.g. an actual investigation performed by forensic accountants). For each of theseaspects, there are four stages, comprising assessment, design, implementation and evaluation.

## C. Investigation approach

**The Investigation Cycle**

So what are the key elements of a forensic investigation?

- Gather, secure and preserve evidence
  - ✓ Computer forensics may need to be involved in order to retrieve the relevant information.
  - ✓ eDiscovery may be involved to identify electronically-stored information in response to a request for production in a law suit or investigation.
- Analyse data
- Check against business intelligence, e.g. -
  - ✓ Does the information gathered appear too good to be true?
  - ✓ Perform background checks on the target, including standing with the government agencies, track records in investing/ gambling activities, litigation history or rumoured criminal links
- Conduct interviews (e.g. looking for additional information from persons whom you believe may have valuable information to offer)
- Report the relevant findings

**Possible next steps after an investigation?**

- Asset tracing, expeditiously “follow the money” and identify where the underlying asset has gone
- Possible professional negligence claims against, for example, auditors
- Presenting expert witness evidence in court, depending on the ability of parties to pay costs/ damages
- Enhancing the internal control and risk management system, to prevent same issues from happening again

## D. Introduction to fraud

- In general, fraud can be categorised into corruption, asset misappropriation, and financial statement fraud. Association of Certified Fraud Examiners has published the fraud tree, summarising different types of frauds in one go.

- The impact of financial statements fraud is much higher than asset misappropriation and corruption.

- Why does fraud occur?

  - ✓ Rationalisation: People who commit frauds try to rationalise it to themselves. For example, staff may overclaim their expenses because all their overtime work has never been adequately compensated for.
  - ✓ Pressure: There could be pressure to meet business targets.
  - ✓ Opportunity: The internal control framework may be vulnerable at the first place.

- Who may be involved in a fraud scheme?

  - ✓ Stakeholders/ creditors
  - ✓ Competitors
  - ✓ Government, e.g. paying bribes to the government officials
  - ✓ Employees
  - ✓ Insurers
  - ✓ Vendors/ suppliers, e.g. overcharging their clients
  - ✓ Customers
  - ✓ Owners/ Managers

- Fraud indicators

| **Accounts** | **Documents** |
|---|---|
| Too good to be true, e.g. significant increase in revenue but without the same in cost of goods sold | Missing or delayed |
| Round-sums | Reluctant to share originals |
| Hostile to auditors | Illegible signature/chop |
| Cash operations | Duplicate document numbers |
| Transactions at unusual times, particularly for those occurring beyond the normal business operating hours | Discrepancies between versions |
| Invoices just below limits, e.g. trying to split the amount of the invoice to circumvent the relevant approval processes | Partial address or PO box |
| Unexpected consultancy fees | Hot off the printer |
| Accounts staff reluctant to take time off | |

## E. Expert witnesses and litigation support

- An expert witness can be anyone with knowledge or experience of a particular field or discipline beyond that to be expected of a layman, including a wide range of professionals e.g. forensic accountants, medical doctors, engineers, auditors, etc., who have expertise in their specific areas.

  It is important to note that the expert witness's duty is to give to the court or tribunal an impartial opinion on particular aspects of matters within his/ her expertise that are in dispute.

- An expert witness:

  - ✓ is retained by a law firm and/or appointed by the court or tribunal to assist in matters beyond the court's or tribunal's expertise.
  - ✓ provides relevant and impartial evidence in his/ her area of expertise. If the concerned expert does not know the answer to a question raised in the courts, he/ she should give a simple response, e.g. "I don't know the answer", without adding personal opinion or speculating.
  - ✓ has in-depth knowledge and relevant experience of the subject matter in dispute.
  - ✓ is able to explain complex matters to the court or tribunal in an understandable manner, and to express his/her professional opinions clearly and honestly, e.g. avoiding jargon.
  - ✓ can disagree or fail to reach the same conclusion as another expert. The court or tribunal will, with the assistance of the evidence of the experts, reach its own conclusion.
  - ✓ should be prepared to change his/ her opinion or make concessions when it is necessary or appropriate to do so, for example, when a new piece of information is available that may question or change the assumptions.

- Roles of expert:

  - ✓ To assist in the preparation of the dispute for arbitration, litigation, or alternative dispute resolution
  - ✓ To prepare an independent expert report
  - ✓ To give evidence to the court/ tribunal, explaining technical matters in dispute; but the expert is not expected to advise on interpretation of law
  - ✓ To assess the strengths and weaknesses of opposing experts
  - ✓ To assist in the preparation of cross-examining the opposition
  - ✓ To act as an arbitrator, mediator, adjudicator

## F. Audit support

- Forensic accounting in support an audit is not the same as an audit. Auditors help provide assurance that a relevant company management is presenting a "true and fair" view of its financial position and performance. In contrast, the scope of a forensic audit is more encompassing than a financial statement audit, in terms of assessing the entity's internal control structure and identification of alleged fraudulent activity or irregularities.